



1998

Oil, Gas and Mineral Law

Richard F. Brown

Follow this and additional works at: <https://scholar.smu.edu/smulr>

Recommended Citation

Richard F. Brown, *Oil, Gas and Mineral Law*, 51 SMU L. Rev. 1219 (1998)
<https://scholar.smu.edu/smulr/vol51/iss4/19>

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in SMU Law Review by an authorized administrator of SMU Scholar. For more information, please visit <http://digitalrepository.smu.edu>.

OIL, GAS AND MINERAL LAW

Richard F. Brown*

TABLE OF CONTENTS

I. INTRODUCTION	1219
II. CONVEYANCING ISSUES.....	1219
III. OIL, GAS AND MINERAL LEASES	1221
A. HABENDUM CLAUSE	1221
B. ROYALTY CLAUSE	1222
C. TOP LEASES	1228
D. SURFACE RIGHTS	1230
E. IMPLIED COVENANTS	1231
IV. DIVISION ORDERS	1233
V. EASEMENTS	1233
VI. LIENS.....	1234
VII. GAS CONTRACTS	1235
VIII. LEGISLATION	1237
A. EXPLORATION AND PRODUCTION	1237
B. ENVIRONMENTAL	1239
C. PIPELINES	1240
D. TAXES	1241
E. GENERAL BUSINESS.....	1243

I. INTRODUCTION

This Article focuses on the interpretations of, and changes relating to, oil, gas and mineral law in Texas from October 1, 1996, through September 30, 1997. The cases examined include decisions of Texas state courts and the Fifth Circuit Court of Appeals.¹

II. CONVEYANCING ISSUES

*Temple-Inland Forest Products Corp. v. Henderson Family Partnership*² is a case involving the mineral/royalty distinction which found that the deeds in question reserved a 1/16 fixed royalty interest rather than a 1/16

* B.A., Rice University; J.D., Southern Methodist University. Attorney-at-Law, Brown & Fortunato, P.C., Amarillo, Texas.

1. This Article is devoted exclusively to Texas law. Cases involving questions of oil, gas and mineral law, decided by courts sitting in Texas, but applying laws of other states, are not included.

2. 958 S.W.2d 183, 184 (Tex. 1997).

mineral interest stripped of appurtenant rights other than the right to receive royalties. The deeds first clearly conveyed an undivided 15/16 of the minerals, and then recited:

In respect to the undivided one-sixteenth (1/16th) part of and interest in the oil, gas and other minerals retained and reserved by the Grantor in said land, it is understood and agreed that said one-sixteenth (1/16th) interest is and shall always be a royalty interest. . . .³

The deeds went on to convey to the grantee as to the reserved interest: (1) the right to develop, (2) the right to lease, (3) the right to bonus, and (4) the right to delay rentals. Thus, of the five attributes of the mineral estate, grantor retained only the right to receive royalty. The issue then was whether this bare royalty right was an attribute of a reserved mineral interest or a 1/16 fixed royalty. The word "royalty" was used six times in each deed.

The Texas Supreme Court determined that *Watkins v. Slaughter*⁴ was controlling. The deed in *Watkins* purported to convey 15/16 of the minerals, and it described the 1/16 retained as an "interest in and to all of the oil, gas and other minerals in and under and that may be produced from said land."⁵ However, the instrument also recited that the grantor "shall receive the royalty retained herein only from actual production. . . ."⁶ The Court concluded in *Watkins* that a royalty had been reserved, and, therefore, the same result must follow when interpreting the Temple-Inland deed.⁷

As to the express recitals in the deeds that the "interest is and shall always be a 'royalty interest,'" the court of appeals had held that such a reference cannot serve to create a royalty interest without an express reference to royalties for *actual production of minerals*.⁸ The appellate court assumed this to be the controlling factor in *Watkins*⁹ and *French v. Chevron U.S.A., Inc.*¹⁰ The Texas Supreme Court reviewed these decisions and others and stated that it has never required that any particular word or phrase be used.¹¹ A mineral conveyance must be considered in its entirety.¹²

This case indicates that the Texas Supreme Court has moved away from "magic words" and from favoring one clause over another in favor of the harmonizing canon of construction. This may not make the job of the title examiner any easier because there are no "bright-line" rules of

3. *Id.*

4. 144 Tex. 179, 189 S.W.2d 699 (1945).

5. *Id.* at 699.

6. *Id.*

7. *See Temple-Inland Forest Prod.*, 958 S.W.2d at 185.

8. *See Temple-Inland Forest Prod. Corp. v. Henderson Family Partnership*, 911 S.W.2d 531, 534-35 (Tex. App.—Beaumont 1996), *rev'd*, 958 S.W.2d 183 (Tex. 1997).

9. *Watkins*, 189 S.W.2d at 699.

10. 896 S.W.2d 795 (Tex. 1995).

11. *See Temple-Inland Forest Prod.* 958 S.W.2d at 186.

12. *See id.*

construction.¹³

III. OIL, GAS AND MINERAL LEASES

A. HABENDUM CLAUSE

In *Hitzelberger v. Samedan Oil Corp.*,¹⁴ the Waco Court of Appeals held that an oil and gas lease terminated for failure to timely pay royalty under an habendum clause with unusual language. The habendum clause provided:

Subject to the other provisions hereof, this lease shall be for a term of Three years from this date (called "Primary Term") and as long thereafter as oil and gas, or either of them, is produced in paying quantities from said land or lands with which said land is pooled hereunder *and the royalties are paid as provided*.¹⁵

The lease was a paid up lease, production was obtained within the primary term, and Samedan failed to timely pay two months of royalties because of a clerical error.

It is the general rule in oil and gas law that failure to make proper and timely royalty payments will not by itself allow the lessor to terminate the lease.¹⁶ This is based on the general concept that the royalty clause is a covenant. In *Hitzelberger*, the obligation to timely pay royalty was included as a part of the habendum clause.

Breach of a condition results in automatic termination of the leasehold estate upon the happening of the stipulated events. Breach of a covenant does not automatically terminate the estate, but instead subjects the breaching party to liability for monetary damages, or in extraordinary circumstances, the remedy of a conditional decree of cancellation.¹⁷

To save its lease, Samedan argued that the requirement to timely pay royalty was a covenant. The court concluded that the lease was unambiguous and that the clear and precise language imposed a condition.¹⁸ Its conclusion was not based on the alleged primacy of the habendum clause as a canon of construction, but upon determining the intention of the parties from the entire lease.¹⁹ Although the court was reluctant to impose a forfeiture, it applied the unambiguous language of the lease to

13. It was believed that "in and under" were magic words defining a mineral interest, that "from actual production" were magic words defining a royalty interest, that the granting clause was more important than other clauses, and that deeds could be analyzed by tracing the splintering of the mineral estate's bundle of sticks ((1) right to develop, (2) right to lease, (3) right to bonus, (4) right to delay rentals, and (5) right to royalty) to define whether the interests examined were minerals or royalties.

14. 948 S.W.2d 497, 502 (Tex. App.—Waco 1997, writ denied).

15. *Id.* at 504 (emphasis added).

16. See, e.g., *Morriss v. First National Bank of Mission*, 249 S.W.2d 269, 279 (Tex. Civ. App.—San Antonio 1952, writ ref'd n.r.e.) (holding that "non-payment of royalty does not terminate a lease, in the absence of a specific clause to that effect") (citation omitted).

17. *Hitzelberger*, 948 S.W.2d at 506.

18. See *id.*

19. See *id.* at 507.

declare the lease terminated.²⁰

B. ROYALTY CLAUSE

The two most important oil and gas cases reported in the 1997 Annual Survey of Texas Law²¹ are perhaps the two most important oil and gas cases in 1998, for a very unusual reason. *Heritage Resources, Inc. v. NationsBank*²² and *Judice v. Mewbourne Oil Co.*²³ were considered at the same time, and the outcome in *Judice* was in part dependent on the more extended reasoning found in *Heritage Resources*. On motion for rehearing in *Heritage Resources*, the Court split four-to-four, and, therefore, the motion was overruled by operation of law.²⁴ On the original opinion, the Court was split 5-2-2, but the majority evaporated on motion for rehearing. Only Justice Baker stayed with the majority opinion. Justice Phillips left the majority and joined the concurring opinion with Justices Owen and Hecht. Justice Enoch left the majority by way of recusal, and Justices Cornyn and Spector joined Justices Gonzalez and Abbot in the dissent on Rehearing.²⁵

The precedential value of *Heritage Resources* and *Judice* are thus severely limited. The dissent on Rehearing wrote:

Because we are without majority agreement on the reasons supporting the judgment, however, the judgment itself has very limited precedential value and controls only this case. Cases relying on the new rule of law pronounced in the Court's April 25, 1996 opinion are similarly restricted. See, e.g., *Judice v. Mewbourne Oil Co.* . . .²⁶

Nevertheless, these issues will not go away, and if anything, litigation will increase, so it is important to revisit *Heritage Resources* and *Judice*²⁷ in the context of the opinion on motion for rehearing in *Heritage Resources*. Obviously, there will be some new faces on the Court before the next case on royalty calculation or post-production costs reaches the Court, but many of the same judges will still be on the Court, and any subsequent case involving these issues will have to consider *Heritage Resources* and *Judice*.

Heritage Resources was intended to clarify the evolution of the law pertaining to division orders and to make definitive some of the law pertaining to the deductibility of post-production costs from royalty.²⁸ The leases involved differed in some respects, but each required that the roy-

20. See *id.* at 509.

21. See Richard F. Brown, *Oil, Gas and Mineral Law*, in *Annual Survey of Texas Law*, 50 SMU L. REV. 1371, 1375 (1997).

22. 939 S.W.2d 118 (Tex. 1996), *reh'g overruled*, 960 S.W.2d 619 (Tex. 1997).

23. 939 S.W.2d 133 (Tex. 1996).

24. *Heritage Resources*, 960 S.W.2d at 619 (Tex. 1997) [hereinafter "Rehearing"].

25. See *id.* at 620.

26. *Id.* (citation omitted); see *Judice*, 939 S.W.2d at 135-36 (citing *Heritage Resources* for the proposition that lessee [sic (lessor)] must share in post-production costs because "[t]he royalty is to be determined based on 'market value at the well'").

27. See *infra* notes 52-58 and accompanying text.

28. See *Heritage Resources*, 939 S.W.2d at 120.

alty for gas sold or used off the premises be based on "market value at the well" and further provided that "there shall be no deductions from the value of Lessor's royalty by reason of any required processing, cost of dehydration, compression, transportation or other matter to market such gas."²⁹ Heritage sold gas off the leased premises. Heritage deducted the cost to transport the gas from the wellhead to the point of sale, as a post-production cost, from the sales price before calculating royalties. NationsBank sued Heritage contending that Heritage deducted transportation costs from the value of NationsBank's royalty in violation of the leases, although NationsBank conceded that the transportation costs deducted were "reasonable." The contested issue was whether Heritage could deduct *any* transportation costs.

Royalty is generally thought to be subject to a proportionate part of post-production costs, including taxes, treatment costs to render the production marketable, and transportation costs.³⁰ Heritage contended that the royalty clause defined the lessor's royalty as a fraction of the market value at the well, and, therefore, reasonable transportation costs should be deducted. NationsBank argued that the lease language specifically prohibited this deduction. The El Paso Court of Appeals agreed with NationsBank and reasoned that Heritage's interpretation would render the post-production clause meaningless.³¹

The majority of the Texas Supreme Court (now reduced to only Justice Baker) agreed that the post-production clause was meaningless, but the Court reversed because the clause was surplusage as a matter of law.³² The majority held that "royalty" and "market value at the well" have commonly accepted meanings in the industry, and by applying those meanings, the post-production clause merely restated existing law.³³ The opinion is significant and is likely to be frequently cited for expressly defining these common industry terms. The definitions are as follows:

Royalty is commonly defined as the landowner's share of production, free of expenses of production. Although it is not subject to the costs of production, royalty is usually subject to post-production costs, including taxes, treatment costs to render it marketable, and transportation costs. However, the parties may modify this general rule by agreement.

Market value at the well has a commonly accepted meaning in the oil and gas industry. Market value is the price a willing seller obtains from a willing buyer. There are two methods to determine market value at the well.

29. *Id.*

30. *See id.* at 122.

31. *See Heritage Resources*, 895 S.W.2d 833, 836-37 (Tex. App.—El Paso 1995), *rev'd*, 939 S.W.2d 118 (Tex. 1996).

32. *See Heritage Resources*, 939 S.W.2d at 122.

33. *See id.* at 122-23.

The most desirable method is to use comparable sales. A comparable sale is one that is comparable in time, quality, quantity, and availability of marketing outlets.

Courts use the second method when information about comparable sales is not readily available. This method involves subtracting reasonable post-production marketing costs from the market value at the point of sale. Post-production marketing costs include transporting the gas to the market and processing the gas to make it marketable. With either method, the plaintiff has the burden to prove market value at the well.³⁴

In the majority opinion, the commonly accepted meanings of these terms in the industry operated to defeat NationsBank's claim.³⁵ The Court reasoned that because the royalty payable was based on "market value at the well" (which necessarily included deductions for post-production costs), a subsequent recital that the "value of the Lessor's royalty" was not reduced by deductions for post-production costs merely restated existing law.³⁶ Nevertheless, because the majority opinion expressly recognized that the meaning of "royalty" could be changed by agreement, a more artfully worded royalty clause could have accomplished the result sought by NationsBank. For example, the result would have likely favored NationsBank if the post-production clause had read:

In determining market value at the well there shall be no deductions from the amount paid to Lessee by the first unrelated third-party purchaser by reason of any required processing, cost of dehydration, compression, transportation or other charge to market such gas, such costs to be borne solely by Lessee.

The concurring opinion discussed at length the meaning of "market value at the well" in the context of determining the amount of royalty payable.³⁷ The two Justices (now four) seem to use "post-production costs" and "marketing costs" interchangeably, and include within that concept marketing costs that may be incurred after the gas leaves the wellhead, such as processing, dehydration, compression, and transportation costs.³⁸ The concurring opinion noted that the issue of deductibility of post-production costs from royalty under a market value royalty clause is an unresolved issue in Texas³⁹ and that other jurisdictions are split.⁴⁰ The concurrence would have adopted what it perceived to be the majority view in Texas and the better-reasoned approach of holding that post-production costs are to be shared by the royalty owner under a "market value at the well" royalty clause, absent language to the contrary.⁴¹

34. *Id.* at 121-22 (citations omitted).

35. *See id.* at 123.

36. *See id.* at 122-23.

37. *See id.* at 124-31.

38. *See id.* at 124.

39. *See id.* at 125-27.

40. *See id.* at 127-29.

41. *See id.* at 126, 129-30.

Contrast this view with the majority opinion's definition of industry terms quoted above. The practical differences could be very significant. Under the majority opinion, faced with a market value royalty clause, the lessee must first determine whether there are comparable sales. This is obviously impractical, uncertain, and an invitation to litigation. If there are no comparable sales, then the lessee must calculate a "net back" price from the actual point of sale by deducting reasonable post-production costs. The concurring opinion described the difficulties in arriving at "market value" as a threshold issue (before considering deductibility of post-production costs), but offered no solution for simplifying that issue.⁴² For as long as Texas jurisprudence continues to support the notion that "market value" is something different than the price that a reasonably prudent lessee is able to obtain while acting in good faith both for himself and for his lessor, there will be no simple solution.⁴³

However, as to post-production costs, the concurring opinion is simple and straight forward. Lessor shares those costs, and they may be proportionately deducted from royalty, unless there is language to the contrary.⁴⁴ Left open is the question: deducted from *what*? If the lessee must first go through the "comparable sales" analysis, there is not much difference between the majority opinion and the concurring opinion. If the concurring opinion is suggesting that market value, absent language to the contrary, is a net back price, then there is a big difference between the opinions and a rational basis for retreating from the morass of uncertainty created by the market value cases. It would be interesting to see the argument presented that market value at the well, for purposes of calculating royalty, in the absence of language to the contrary, is the price that a reasonably prudent lessee is able to obtain while acting in good faith both for himself and for his lessor, less a proportionate part of post-production costs.

The concurring opinion agreed with the majority in finding that the prohibition against deductions from the value of lessor's royalty was surplusage.⁴⁵ The dissent held that the language clearly stated that no post-production costs are to be deducted from what would otherwise be payable as royalty based on market value at the well.⁴⁶ The dissent offers little guidance on the general issue of the deductibility of post-production costs because these *particular* royalty clauses, in its opinion, make all such costs non-deductible.⁴⁷

Heritage Resources is also an important division order case. In the El Paso Court of Appeals, the division order issues were more important

42. See *id.* at 125-26.

43. See *First Nat'l Bank v. Exxon Corp.*, 622 S.W.2d 80 (Tex. 1981); *Exxon Corp. v. Middleton*, 613 S.W.2d 240 (Tex. 1981); *Texas Oil & Gas Corp. v. Vela*, 429 S.W.2d 866 (Tex. 1968).

44. See *Heritage Resources*, 939 S.W.2d at 130.

45. See *id.* at 131.

46. See *id.*

47. See *id.* at 130-31.

because Heritage's first defense—that post-production costs are deductible under the royalty clauses—failed, and Heritage urged a second defense based on division orders, which allowed the deduction of transportation costs. Under the interpretation given to the royalty clauses by Heritage and by the Texas Supreme Court, the provisions of the division orders were no longer as important because those provisions were essentially consistent with the royalty clauses in the leases.⁴⁸ Nevertheless, the Texas Supreme Court expressly disapproved of portions of the appellate court's opinion that conflicted with *Gavenda v. Strata Energy, Inc.*⁴⁹

Heritage Resources clarifies the result when division orders prepared by the operator incorrectly allocate payments among the interest owners in a manner that differs from the lease provisions and the operator retains a benefit. The division orders are not binding, and the operator is liable for the benefit retained, but only the benefit retained, on the principle of unjust enrichment.⁵⁰ In other words, the lessee who overpays himself at the expense of the royalty owner signing the division order cannot hide behind the division order. If the wrongful payment has gone to someone else, the lessee can hide behind the division order. Any other result would defeat the utility of the division order in expediting payments and would further delay the orderly resolution of title issues. This part of the decision should be very helpful in reducing the confusion about the effectiveness of division orders, and neither the concurring opinion nor the dissenting opinion in *Heritage Resources* addressed the issue of division orders, presumably making the Court unanimous on this issue. To recover any payments made under a division order prior to revocation, the remedy must be pursued against the party that ended up with the money, and a claim can be pursued against that party only to the extent of the money that party received.⁵¹ It is a bright-line, a distinctive line, and it fits within the well-established legal doctrine of unjust enrichment.

In clarifying the effect of division orders, the decision is a good one. It is hard to see how any party could complain. Don't sign a division order and accept benefits, unless you are sure of your own interest. Once pay-

48. See *id.* at 123.

49. See *id.* at 123 (citing *Gavenda*, 705 S.W.2d 690 (Tex. 1986)).

50. See *id.* In *Gavenda*, the case was remanded for a determination of the amount of royalty owed by Strata and the other working interest owner. Strata was only liable for whatever position of the royalties it retained and was not liable for any royalties it paid out to other owners. *Gavenda*, 705 S.W.2d at 692-93. Thus, *Gavenda* stands for the premise that if the issuer of the division order makes a mistake in the issuer's favor (and does not pay it over to another), then the issuer must give up its unjust enrichment to the rightful owner. Presumably, the same recovery based on unjust enrichment would be available against any overpaid party. The critical fact issue is to determine who received the overpayment. This simple concept was unfortunately and unnecessarily confused by a poorly reasoned opinion on remand in *Strata Energy, Inc. v. Gavenda*, 753 S.W.2d 789 (Tex. App.—Houston [14th Dist.] 1988, no writ), which held that the operator was liable for overpayment made to overriding royalty owners because it was a benefit "retained" by the working interest owner, although the money was paid out to the overriding royalty owners. *Heritage Resources* effectively disapproved the *Gavenda* opinion on remand on this issue.

51. See *Heritage Resources*, 939 S.W.2d at 123.

ments are made, you cannot recover for an underpayment against anyone except the party receiving the unjust enrichment. As to "market value" and "post production costs," this case will be dissected by lawyers for years. In an era of gathering system spinoffs and increasing gathering costs, this will be an area of litigation for some time.

In *Judice v. Mewbourne Oil Co.*,⁵² Mewbourne deducted a pro rata part of post-production compression costs from lessor's royalty. The royalty under the leases was to be a fractional part of the "market value at the well" of the gas produced. Relying upon *Heritage Resources*,⁵³ decided the same day, the Texas Supreme Court held that under a market value royalty clause, the royalty is payable net of any value added by compressing the gas after it leaves the wellhead.⁵⁴ Therefore, Mewbourne was entitled under its leases to allocate to the royalty owners their proportionate share of the reasonable costs of post-production compression.⁵⁵

Having settled the meaning of the royalty clause with respect to post-production compression costs, the Court turned to the effect to be given to division orders executed by the lessors. One form of division order provided that settlement was to be based on "net proceeds realized at the well" and deleted all of the rest of the form, which expressly allowed deductions for compression costs.⁵⁶ The Court held that "net proceeds" expressly contemplates deductions and that its interpretation of "at the well" means before value is added by preparing the gas for market.⁵⁷ The handwritten deletions did not change what was left in the division order, so under this division order, compression costs were deductible. A second form of division order provided that settlement was to be based on "gross proceeds realized at the well." The Court concluded that this form was ambiguous and did not upset a jury finding that the parties intended that royalty was to be payable without deductions for compression.⁵⁸

*Amoco Production Co. v. Smith*⁵⁹ considered the statute of limitations applicable to the recovery of royalty overpayments in an action brought by a lessee and whether that lessee could recover attorney's fees. Amoco listed both Herbert W. Smith and Huling W. Smith on its records as "H. W. Smith," resulting in overpayment to Herbert and underpayment to Huling for years. Amoco reimbursed Huling and sued Herbert for the overpayment. The issue was whether the two-year or four-year statute of limitations would be applicable.⁶⁰

52. 939 S.W.2d 133 (Tex. 1996).

53. See *supra* notes 26-51 and accompanying text.

54. See *Judice*, 939 S.W.2d at 134.

55. See *id.* at 135.

56. See *id.*

57. See *id.* at 137.

58. See *id.*

59. 946 S.W.2d 162 (Tex. App.—El Paso 1997, no writ).

60. See *id.* at 163.

The claim was characterized as a cause of action for money had and received, which conceptually falls within the doctrine of unjust enrichment. "Unjust enrichment is not an independent cause of action but rather characterizes the result of a failure to make restitution of benefits under circumstances which give rise to an implied or quasi-contractual obligation to return the benefits."⁶¹ The law implies a contract, and it is, therefore, a contract cause of action for debt not evidenced by a writing.⁶²

At one time, Texas had a two-year statute of limitations applicable to oral contracts and a four-year statute applicable to written contracts.⁶³ It was, therefore, uniformly held that the two-year statute of limitations was applicable to suits for unjust enrichment.⁶⁴ However, the limitation statute was amended in 1979 and continues to provide that all actions for debt will be under the four-year statute.⁶⁵ The statute of limitations applicable to this cause of action is now four years.⁶⁶

The trial court declined to award attorney's fees to Amoco, and on appeal, the El Paso Court of Appeals refused to reverse the trial court's decision, noting that the standard of review is abuse of discretion. The appellate court was apparently persuaded that the refusal to award attorney's fees was supportable because the overpayment was attributable to Amoco's own mistake.⁶⁷ Of more significance is the court's conclusion that attorney's fees could be awarded in a proper case under section 38.001 of the Texas Civil Practice and Remedies Code as a suit based on a contract, even though the contract is neither written nor oral, but implied.⁶⁸

C. TOP LEASES

*Santa Fe Energy Operating Partners, L.P. v. Carrillo*⁶⁹ supports the actions of a lessee in taking protection leases from other parties while holding a lease from the adverse possessor. Carrillo's record title, for various reasons, was only partially good. As to portions of his land, he was dependent upon adverse possession to support his title. Carrillo leased to Santa Fe. Santa Fe took protection leases from some of the other claimants. The Carrillo/Santa Fe lease expired, and Carrillo refused to extend the lease. Negotiations with another prospective lessee broke down because of the Santa Fe leases with the record title holders. Carrillo sued Santa Fe and the record title holders for slander of title and tortious inter-

61. *Id.* at 164.

62. *See id.*

63. *See id.* at 164.

64. *See id.*

65. *See* TEX. CIV. PRAC. & REM. CODE ANN. § 16.004 (Vernon 1986).

66. *See Amoco Prod.*, 946 S.W.2d at 165.

67. *See id.* at 166.

68. *See id.* at 165-166. TEX. CIV. PRAC. & REM. CODE ANN. § 38.001 (Vernon 1997) provides in pertinent part: "A person may recover reasonable attorney's fees from an individual or corporation, in addition to the amount of a valid claim and costs, if the claim is for: . . . (8) an oral or written contract."

69. 948 S.W.2d 780 (Tex. App.—San Antonio 1997, no writ).

ference with prospective business relations. The record title holders settled by executing quit claim deeds to Carrillo.

One of the defenses to a tortious interference claim is that the party interfering is justified.⁷⁰ "Santa Fe's actions would be justified if it had a right to interfere with the prospective contract as a matter of law or if it had a colorable legal right it exercised in good faith."⁷¹ The appellate court found the necessary legal justification in the Carrillo/Santa Fe lease, which contained a proportionate reduction clause clearly contemplating that Carrillo might own less than the entire undivided fee and providing for the consequences.⁷² The court held that Santa Fe had the right to protect itself by taking leases from adverse claimants, "actual or potential,"⁷³ relying on *Shell Oil v. Howth*.⁷⁴ The opinion went further than *Shell Oil* because Santa Fe had protected itself as to one small tract by acquiring a quit claim deed, rather than a lease. The court reasoned that under these circumstances, a protection lease may take the form of a quit claim or an ordinary lease.⁷⁵ As to tortious interference, the court reversed and rendered.⁷⁶

Carrillo's related claim of slander of title also failed. Slander of title requires "malice," which is defined as making false statements regarding title in the absence of color of title or a reasonable belief that the parties have title.⁷⁷ Given that Santa Fe was entitled to execute the protection leases as a matter of law, then, also as a matter of law, Santa Fe reasonably believed the record owners held title.⁷⁸ As to slander of title, the court reversed and rendered.⁷⁹

Because the court affirmed limitations title in Carrillo, it also let stand the award of \$133,837 in attorney's fees against Santa Fe.⁸⁰ Left unresolved was whether an adverse possessor could bring claims of tortious interference and slander of title. Although Santa Fe urged this issue, the court assumed without deciding that Carrillo could bring such claims because the court found that Santa Fe's actions were lawful.⁸¹

70. *See id.* at 784.

71. *Id.*

72. *See id.* at 785.

73. *Id.*

74. 138 Tex. 357, 159 S.W.2d 483, 489 (1942).

75. *See Santa Fe Energy*, 948 S.W.2d at 785.

76. *See id.* at 782, 785.

77. *See id.* at 785.

78. *See id.*

79. *See id.*

80. *See id.* at 786-87.

81. *See id.* at 784. Santa Fe argued that, at the time of trial, Carrillo held an unperfected adverse possession claim and that such a claim could not be interfered with or slandered as a matter of law. The court cited conflicting authority from other jurisdictions regarding whether such claims could be brought by the adverse possessor. *See id.* at 784 n.1.

D. SURFACE RIGHTS

*Landreth v. Melendez*⁸² held that the "accommodation doctrine,"⁸³ which balances the rights of the mineral owner and the surface owner, is not applicable when the rights of the mineral owner arise under a prior express reservation of easement rights, rather than the implied rights arising under an oil and gas lease.⁸⁴ At issue between the surface owner and the mineral lessee was whether the lessee was required to accommodate the surface owner's center pivot irrigation system by using low profile pumping units rather than conventional pumping units.

The prior express reservation of easement rights reserved to the mineral owner the right:

. . . to take all usual, necessary and convenient means for working, preparing, getting out and removing said oil, gas and other minerals It is expressly understood that there shall be no liability on the part of [mineral owner], their heirs and assigns to [surface owner], their heirs and assigns, for damages to the surface estate in the hereinbefore described land in connection with the testing, drilling, producing and marketing of oil, gas and other minerals from the hereinbefore described land *as aforesaid*.⁸⁵

Thus, the surface owner was on notice that the mineral owner reserved the right to use all "usual, necessary and convenient means" to develop the minerals, and absent negligence, without liability to the surface owner.⁸⁶

The case expressly distinguished its holding from *Getty Oil*⁸⁷ by noting that the rights of the mineral owner are to be determined by the interpretation of the prior mineral reservation, rather than implied from an oil and gas lease.⁸⁸ This distinction is important because there are many recorded deeds reserving mineral rights in which the draftsmen have elaborately described the easement rights. Many attorneys would have considered this to be redundant and poor draftsmanship when the mineral estate is the unchallenged "dominant" estate. If the scope of the easement rights now turns on express rather than implied easement rights, then perhaps the poor draftsman was the careful (or perhaps prescient) draftsman. Similarly, those lessees claiming under leases with elaborately drafted granting clauses, including expansive easement rights,

82. 948 S.W.2d 76 (Tex. App.—Amarillo 1997, no writ).

83. The "accommodation doctrine" is used to describe the relationship between the mineral owner's dominant estate and the surface owner's servient estate. It generally means that the dominant estate is not simply dominant, but the rights of the mineral estate must be exercised so as to strike a balance between the interests of both the surface owner and the mineral owner. See *Sun Oil Co. v. Whitaker*, 483 S.W.2d 808, 810-12 (Tex. 1972). For a case with remarkably similar facts to *Landreth* in terms of surface usage and that applies the accommodation doctrine, see *Getty Oil Co. v. Jones*, 470 S.W.2d 618 (Tex. 1971).

84. See *Landreth*, 948 S.W.2d at 81.

85. *Id.* at 78-79 (emphasis added).

86. *Id.* at 81.

87. 470 S.W.2d at 621-22; see *supra* note 83.

88. See *Landreth*, 948 S.W.2d at 81.

may be in a superior (dominant?) position compared to lessees claiming under simple grants to explore, develop and produce.

E. IMPLIED COVENANTS

In *Neel v. HECI Exploration Co.*,⁸⁹ the court examined the duties owed by a lessee to a lessor when the reservoir is damaged by a third party. Neel leased to HECI, which drilled wells, produced oil, and paid royalties. AOP Operating Corporation was producing excessively from the same field by overproducing a well on adjacent acreage. HECI complained to the Railroad Commission three times, but AOP continued to produce. The overproduction resulted in damages to the reservoir and lost reserves. HECI sued AOP and recovered \$1,719,956 in actual damages and \$2,000,000 in punitive damages, together with injunctive relief. Neel, the owner of the surface and a royalty interest owner, did not have actual knowledge of the suit until long after its conclusion. HECI refused to share the judgment with Neel.

Neel sued HECI for breach of the contract to pay royalty, negligent misrepresentation, breach of the implied covenant to protect the leasehold, an accounting, unjust enrichment, and punitive damages. The trial court granted HECI a summary judgment. On appeal of the summary judgment, analysis was complicated by the fact that the record on HECI's judgment against AOP was unclear as to whether the judgment against AOP was for 5/6 or 6/6 of the lost reserves and reservoir damage.⁹⁰

Although Neel's rights in the oil were transferred under the lease to HECI,⁹¹ Neel still retained an interest in reserves sufficient to give him a cause of action against AOP.⁹² The record was silent as to whether Neel had done anything to proceed against AOP. At issue were the duties owed by HECI to Neel for the damages caused by AOP, particularly under the royalty clause and the implied covenant to protect the leasehold. Neel contended that HECI should have sued AOP on his behalf, while HECI argued that it could not sue on Neel's behalf without an assignment of the cause of action.

The court concluded that if HECI recovered against AOP for the entire 6/6 without having to carve out a royalty share, then part of the recovery would be at Neel's expense.⁹³ If HECI failed to recover for Neel's share, then, under the doctrine of collateral estoppel, Neel could be precluded

89. 942 S.W.2d 212 (Tex. App.—Austin 1997, writ granted).

90. See *id.* at 220.

91. The lost production was apparently oil, rather than gas, although the opinion does not make this completely clear. Assuming that the production was oil, the court's assertion that Neel's rights in the oil were conveyed to HECI under the lease would not ordinarily be true. The typical lease form conveys the gas, reserving only a royalty, but reserves the right to take the royalty share of the oil in kind. The court's analysis of the relationships of the parties and the oil is sketchy, and it is entirely possible that different duties and liabilities would arise under different royalty clauses as to gas, rather than oil.

92. See *id.* at 216.

93. See *id.* at 217.

from an independent recovery.⁹⁴ Although the court agreed that HECI could not sue on behalf of Neel without Neel's consent, it concluded that the lessee's duty at least required the lessee to give timely notice to Neel.⁹⁵ Neel could then sue, assign the right to sue, or waive his rights.⁹⁶ The court stated:

We hold that a mineral lessee who determines that a suit for damages is necessary to protect the leasehold, but lacks the power to sue for all who have interests in the leasehold, must notify the unrepresented interest-holders of the need for suit and the lessee's intent to sue. This is not a new implied duty, but a specific means to fulfill the existing implied covenant to protect the leasehold. Our holding recognizes the lessee's duty to protect the entire leasehold, not just its own share of the theoretic production.⁹⁷

The court was careful to note that the duty to notify imposed on the lessee would not create any liability as to the lessor who had independent knowledge of the need for a suit.⁹⁸

Liability for lost production does not conflict with cases holding that no royalty was payable on take-or-pay agreements. Although those cases hold that royalty is only payable by lessee on *actual* production, liability in *Neel* is based on the value of reserves which will never be produced by the lessee. Although recovery cannot be for *royalty* under the royalty clause, the recovery may be measured by the lost royalty.⁹⁹ Therefore, the summary judgment denying recovery on the contractual claim for royalty was affirmed, but the denial of the contractual claim for breach of the implied covenant to protect the leasehold was reversed and remanded.¹⁰⁰

HECI's motion for summary judgment failed to address the allegation of negligent misrepresentation based on HECI's failure to inform Neel and its unilateral decision to sue, so that issue was also remanded.¹⁰¹ Similarly, the summary judgment record was not complete on the unjust enrichment claim.¹⁰²

The *Neel* opinion is also important for its discussion of the relationship between the causes of action asserted, the statutes of limitation, and the discovery rule. The court relied on the recent case of *S.V. v. R.V.*¹⁰³ to define the two critical elements involved in balancing the benefits of precluding stale claims versus the risks of precluding meritorious claims. Those two elements are "inherent undiscoverability" and "objective

94. *See id.* at 217 n.1.

95. *See id.* at 217-18.

96. *See id.*

97. *Id.* at 218.

98. *See id.* at 219.

99. *See id.*

100. *See id.* at 223.

101. *See id.* at 219-20.

102. *See id.* at 220.

103. 933 S.W.2d 1, 6-7 (Tex. 1996).

verifiability."¹⁰⁴

The *Neel* court recognized that Neel's injury was objectively verifiable, but the more difficult question was whether the injury was inherently undiscoverable.¹⁰⁵ Notwithstanding the public nature of the Railroad Commission, the state court proceedings and various public filings, Neel had no reason to inquire or to be suspicious and had no actual knowledge of the overproduction or the judgment. Therefore, the discovery rule was applicable because the wrong and the injury were unknown to the plaintiff due to no fault of his own.¹⁰⁶ The court was careful to distinguish cases holding otherwise on a failure to pay royalty claim under circumstances where the royalty owner had actual knowledge.¹⁰⁷

IV. DIVISION ORDERS

The two most important division order cases, *Heritage Resources* and *Judice*, are discussed above in Section III.B.

V. EASEMENTS

*Orange County, Inc. v. Citgo Pipeline Co.*¹⁰⁸ considered the alienability of a partial interest in a pipeline easement. In 1943, an easement was granted to Citgo's predecessor for a twelve-inch pipeline which was constructed. In 1952, an easement was granted to Citgo for the construction, maintenance, and operation of "pipelines," providing that additional compensation would be paid for each additional pipeline. A twenty-inch pipeline was constructed. In 1987, Citgo assigned the twelve-inch pipeline and an undivided one-half interest in the easement. Orange County contended that the easement could not be partially assigned.

Although there may be a conflict in Texas law, the Beaumont Court of Appeals adopted what it called the modern view: that commercial easements are partially alienable when the assignment does not burden the underlying land beyond what was contemplated in the original easement grant.¹⁰⁹ The court cited but did not expressly adopt section 493 of the *Restatement of Property*.¹¹⁰ The court held that the easement contemplated multiple pipelines, that each pipeline triggered additional compensation to the servient estate, and that the owner of the servient estate had presented no evidence of any additional burden.¹¹¹

Orange County contended that the easement was not an exclusive easement, and, therefore, apportionability of the easement should not be assumed in the absence of a clear indication to the contrary. The court

104. *Id.*

105. *See Neel*, 942 S.W.2d at 221.

106. *See id.*

107. *See id.* at 222.

108. 934 S.W.2d 472 (Tex. App.—Beaumont 1996, writ denied).

109. *See id.* at 475.

110. *See* RESTATEMENT OF PROPERTY § 493 (1944).

111. *See Citgo Pipeline*, 934 S.W.2d at 476-77.

rejected this argument and held that the easement was an exclusive easement in gross as to pipelines.¹¹² It quoted with approval the following language from the *Restatement*:

Though apportionability may be to the disadvantage of the possessor of the servient tenement, the fact that he is excluded from making the use authorized by the easement, plus the fact that apportionability increases the value of the easement to its owner, tends to the inference in the usual case that the easement was intended in its creation to be apportionable. This inference is very strong in cases where an increase in use is in fact advantageous to the possessor of the servient tenement.¹¹³

VI. LIENS

*Abella v. Knight Oil Tools*¹¹⁴ considered whether the holders of mechanic's liens can divert the proceeds of current production into the registry of the court *prior to* foreclosure of the liens. In this consolidated case, multiple holders of statutory mechanic's and materialmen's (M&M) liens¹¹⁵ provided labor and materials to the operator for drilling, completing, maintaining, operating, and repairing three wells. The lien holders were not paid in full for their services and timely perfected their M&M liens against the operator. The operator assigned the leasehold to other working interest owners. In the foreclosure action, the lien holders sought the appointment of a receiver to collect and hold the proceeds of production until the liens could be foreclosed. The assignee working interest owners argued that they were entitled to the current production proceeds until the liens were actually foreclosed, even if this meant the oil and gas reserves became totally depleted. The trial court agreed with the lien holders and appointed a receiver *prior to* the actual foreclosure to collect the net proceeds of production from the wells and to deposit those proceeds with the court.

The statute upon which the M&M liens are based clearly extends to the equipment and material placed on the lease, and it also covers "the land, leasehold, oil or gas well, . . . and lease for oil and gas purposes for which the labor was performed"¹¹⁶ The statute is silent as to whether the lien extends to oil and gas produced prior to foreclosure or the proceeds from its sale. The court held that the M&M liens attached not only to the materials supplied, but also to the leaseholds, and that the "leases grant the right to extract and produce the oil and gas from the land."¹¹⁷ The majority of the court apparently concluded that this demonstrated a probable right of recovery, and it declined to reverse the trial court's ap-

112. See *id.* at 476.

113. RESTATEMENT OF PROPERTY § 493.

114. 945 S.W.2d 847 (Tex. App.—Houston [1st Dist.] 1997, no writ).

115. See TEX. PROP. CODE ANN. § 56.003 (Vernon 1995).

116. *Abella*, 945 S.W.2d at 850.

117. *Id.* at 851.

pointment of a receiver.¹¹⁸

The dissent argued that lien statutes must be strictly construed, that this statute does not expressly extend to proceeds, and that, at most, it extends to the operator's right to extract production.¹¹⁹ Because no injunction was sought, production should have continued, and the proceeds of production should be free from liens.¹²⁰

VII. GAS CONTRACTS

*Condra v. Quinoco Petroleum, Inc.*¹²¹ is another *en banc* opinion out of the San Antonio Court of Appeals considering rights to share in take-or-pay settlements received by a lessee and the effect of division orders.¹²² The San Antonio Court of Appeals continues to closely follow the bright-line rule that royalties are generally payable only on gas actually produced.¹²³ In *Condra*, lessee settled a take-or-pay claim for both a substantial recoupable payment and a substantial nonrecoupable payment. The recoupable payment was essentially a prepayment for gas to be produced in the future. The nonrecoupable payment was attributable to the settlement of certain other claims and the amendment of the gas purchase contract to make the contract more favorable for the gas purchaser. Lessee refused to share either payment with the overriding royalty owners.

The overriding royalty owners claimed that they were entitled to share in the settlement under the terms of the division orders. The claim was denied by reference to the express language of the division orders, which recited that payment was to be made on "all proceeds derived from the sale of products produced from or attributable to said property. . . ."¹²⁴ The majority held that "attributable to" modified "products," and, therefore, the case was indistinguishable from its prior opinion in *Hurd Enterprises, Ltd. v. Bruni*,¹²⁵ which held that royalty was payable only on gas actually produced. Although the dissent argued that *Condra* was distinguishable from *Hurd Enterprises*, because in *Condra* there was a nonrecoupable payment,¹²⁶ the majority found that a nonrecoupable pay-

118. *See id.*

119. *See id.* at 852.

120. *See id.*

121. 954 S.W.2d 68 (Tex. App.—San Antonio 1997, no writ).

122. *See TransAmerican Natural Gas Corp. v. H.S. Finkelstein*, 933 S.W.2d 591, 593 (Tex. App.—San Antonio 1996, writ denied) (repudiation damages under take-or-pay contract for gas not taken when there was subsequent production); *Hurd Enters., Ltd. v. Bruni*, 828 S.W.2d 101, 103 (Tex. App.—San Antonio 1992, writ denied) (take-or-pay payments in lieu of takes).

123. *See Condra*, 954 S.W.2d at 71.

124. *Id.*

125. 828 S.W.2d at 106.

126. *See Condra*, 954 S.W.2d at 74-78. Part of the problem with following the reasoning and opinions of the San Antonio Court of Appeals is that *Finkelstein* was first issued and withdrawn as a panel opinion before finally being issued with the panel opinion relegated to the dissent, and *Condra* was issued while writ was still pending in *Finkelstein*. In *Con-*

ment was indistinguishable from repudiation damages.¹²⁷ The majority of the court found its own opinion on repudiation damages in *TransAmerican Natural Gas Corp. v. Finkelstein*¹²⁸ to be controlling, and, therefore, no overriding royalty was payable on the nonrecoupable payment.¹²⁹ The dissent argued that royalty should be payable on nonrecoupable take-or-pay settlements.¹³⁰

The overriding royalty owners also sought to recover under the express and implied covenants to market. As to overriding royalty owners, these covenants do not arise under the lease, but under the assignment creating the overriding royalty. The overriding royalty owner cannot enforce the lessor's lease covenants.¹³¹ Although there is an implied covenant to market in the assignment creating an overriding royalty, the implied covenant to market arising under the assignment is not triggered in the absence of actual production.¹³² The terms of the underlying oil and gas lease with respect to the obligation to market do not negate or restrict the breadth of the covenant implied in the assignment.¹³³

The dissent argued that the implied covenant to market arising under the assignment is applicable to the negotiation of a gas contract and is equally applicable to the renegotiation of that contract in the form of a settlement agreement regarding a take-or-pay contract.¹³⁴

*Northern Natural Gas Co. v. Conoco, Inc.*¹³⁵ construed a natural gas transportation and processing agreement as to the intent of the dedication of reserves and whether the gas purchaser could unilaterally terminate gas purchase contracts and escape the obligation to deliver gas. Northern purchased gas from producers for delivery into Conoco's gas processing and gathering facilities. The agreement was to continue "for so long as the various Gas Purchase Contracts dedicated hereunder remain in effect, but not less than twenty (20) years, unless terminated pursuant to the terms herein."¹³⁶ Northern agreed to deliver, and Conoco agreed to accept, "all gas for gathering, compressing and processing in keeping with all the quantity and other provisions of [Northern's] various gas purchase contracts in effect from time to time."¹³⁷

As the Federal Energy Regulatory Commission proceeded with the deregulation of gas marketing, Northern began canceling and buying out its contractual obligations to purchase gas from producers. By 1990, North-

dra, both sides of the nonrecoupable payment issue were again arguing their own *Finkelstein* position.

127. *See id.* at 71.

128. 933 S.W.2d at 596-97.

129. *See Condra*, 954 S.W.2d at 73.

130. *See id.* at 74-75.

131. *See id.* at 72.

132. *See id.* at 72-73. The court again relied upon its own opinion in *Finkelstein*, 935 S.W.2d at 598.

133. *See Condra*, 954 S.W.2d at 72.

134. *See id.* at 76.

135. 939 S.W.2d 676 (Tex. App.—El Paso 1996, writ granted).

136. *Id.* at 678.

137. *Id.*

ern was no longer purchasing gas from these producers and was acting only as a gas transporter. Conoco contended that Northern was obligated to continue purchasing all of the gas produced from the wells listed in the agreement and to deliver that gas to Conoco for the productive life of the wells. Conoco obtained a favorable jury instruction, a finding of breach by the jury, and a judgment for over \$20,000,000 in damages for lost gas processing profits.

The court of appeals concluded that the agreement was unambiguous and that it did not require Northern to deliver all natural gas reserves from dedicated wells for the productive life of the wells.¹³⁸ Northern was required to make deliveries only for so long as the gas purchase contracts remained in effect.¹³⁹

The court reversed but did not render for Northern. Conoco contended that Northern's contract cancellations were contrary to the good faith standard of section 1.203 of the Texas Business and Commerce Code¹⁴⁰ and Texas case law holding that every contract includes an element of confidence and trust requiring each party to faithfully perform his obligations under the contract.¹⁴¹ Concluding that nothing in the agreement permitted Northern to cancel all of the contracts in bad faith, the court remanded on the fact question of good faith.¹⁴²

VIII. LEGISLATION

The following is a brief summary of the new legislation adopted by the 75th session of the Texas Legislature. The new legislation covers areas of exploration and production, environmental law, pipelines, taxes, and general business issues.

A. EXPLORATION AND PRODUCTION

1. ACT: Act of May 26, 1997, 75th Leg., R.S., ch. 299, 1997 Tex. Sess. Law Serv. 1322 (Vernon).¹⁴³
- ISSUE: Definition of a marginal gas well.
- SUMMARY: This Act gives the Railroad Commission the authority to exempt certain individual marginal gas wells from otherwise applicable production limitations. A marginal well is incapable of producing, under normal operating conditions, more than 250,000 cubic feet of gas per day; however, no portion of this law shall require production to be limited from a marginal gas well if the well (1) has a daily deliverability of 100,000

138. *See id.* at 680.

139. *See id.*

140. *See* TEX. BUS. & COM. CODE ANN. § 1.203 (Vernon 1994).

141. *See Northern*, 939 S.W.2d at 680 (citing *Crim Truck & Tractor Co. v. Navistar Int'l Transp. Corp.*, 823 S.W.2d 591, 595 (Tex. 1992)).

142. *See id.* at 681 (citing *Lenape Resources Corp. v. Tennessee Gas Pipeline Co.*, 925 S.W.2d 565, 571 (Tex. 1996)).

143. To be codified as an amendment to TEX. NAT. RES. CODE ANN. § 86.091.

cubic feet of gas or less or (2) is in a field for which special field rules are not in effect.

Effective: May 26, 1997.

2. ACT: Act of May 21, 1997, 75th Leg., R.S., ch.198, 1997 Tex. Sess. Law Serv. 1065 (Vernon).¹⁴⁴
 ISSUE: Disposition by the Railroad Commission of well-site equipment from a wellbore transferred to the Texas Experimental Research and Recovery Activity (TERRA).
 SUMMARY: This Act provides that the Railroad Commission may dispose of abandoned equipment from TERRA well-sites for both human safety and pollution concerns. The Act also provides that the property may be removed in a commercially reasonable manner.
 EFFECTIVE: September 1, 1997.
3. ACT: Act of May 15, 1997, 75th Leg., R.S., ch. 88, 1997 Tex. Sess. Law Serv. 175 (Vernon).¹⁴⁵
 ISSUE: The status of certain oil and gas workers or service providers as independent contractors.
 SUMMARY: This law resolves questions over the status of sole proprietors, without employees, who are hired as independent contractors to perform services on oil and gas wells. Before this law, the oil and gas well operator was required to provide workers' compensation insurance for these persons. Under the new law, sole proprietors are to be treated in the same manner as independent contractors with employees and are not entitled to coverage under the operator's workers' compensation insurance policy unless agreed to by both parties.
 EFFECTIVE: September 1, 1997.
4. ACT: Act of May 15, 1997, 75th Leg., R.S., ch. 89, 1997 Tex. Sess. Law Serv. 176 (Vernon).¹⁴⁶
 ISSUE: Responsibility for the plugging of an oil or gas well.
 SUMMARY: An operator, defined as a person who assumes responsibility for the physical operation and control of an oil well, must be designated and accepted by the Railroad Commission. Also, the operator must have a Railroad Commission-approved form of financial security for the operation of the oil well. Section 2 of the Act provides that the duty of a person to plug an unplugged well that has ceased operation ends only when the person's interest is sold while the well is in compliance with the Railroad Commission's safety and pollution rules.

144. To be codified as an amendment to TEX. NAT. RES. CODE ANN. § 93.013.

145. To be codified at TEX. LABOR CODE ANN. § 406.123(h).

146. To be codified as an amendment to TEX. NAT. RES. CODE ANN. §§ 89.002(2)(a), 89.011(b).

EFFECTIVE: September 1, 1997.

5. ACT: Act of May 19, 1997, 75th Leg., R.S., ch. 121, 1997 Tex. Sess. Law Serv. 231 (Vernon).¹⁴⁷
- ISSUE: Acceptance, approval, or revocation by the Railroad Commission of organizational reports, applications for permits, or certificates of compliance.
- SUMMARY: This Act provides that the Railroad Commission may not approve an organizational report and may not issue a certificate of compliance if the organization has an outstanding violation or if a person holding a position of ownership or control has within the past five years held a position of ownership or control in another organization which has an outstanding violation. The Act also prohibits any entity from performing any operation within the jurisdiction of the Railroad Commission without maintaining a valid organizational report and proof of financial security on file with the Railroad Commission.
- EFFECTIVE: September 1, 1997.

B. ENVIRONMENTAL

1. ACT: Act of May 26, 1997, 75th Leg., R.S., ch. 286, 1997 Tex. Sess. Law Serv. 1301 (Vernon).¹⁴⁸
- ISSUE: The disposal or temporary storage of litter or solid waste.
- SUMMARY: This provision amends the definition of "approved solid waste site" to include a solid waste site registered with the Texas Natural Resources Conservation Commission. The Texas Natural Resources Conservation Commission shall regulate temporary storage for future disposal of solid waste as well.
- EFFECTIVE: May 26, 1997.
2. ACT: Act of June 20, 1997, 75th Leg., R.S., ch. 1373, 1997 Tex. Sess. Law Serv. 5158 (Vernon).¹⁴⁹
- ISSUE: Consolidated permit processing by the Texas Natural Resources Conservation Commission.
- SUMMARY: This statute explains the availability and requirements of the consolidated permit process. This legislation was necessary due to unintended changes when the Texas Air Control Board and Texas Water Commission were consolidated. The agency now in charge of this permit process will be the Texas Natural Resources Conservation Commission.
- EFFECTIVE: September 1, 1997.

147. To be codified at TEX. NAT. RES. CODE ANN. § 91.142(e), (f) and as an amendment to § 91.114.

148. To be codified at TEX. HEALTH & SAFETY CODE ANN. § 365.012(k) and as an amendment to §§ 365.011(1), 365.012(j).

149. To be codified at TEX. WATER CODE ANN. § 5(J).

3. **ACT:** Act of May 21, 1997, 75th Leg., R.S., ch. 206, 1997 Tex. Sess. Law Serv. 1074 (Vernon).¹⁵⁰
- ISSUE:** Environmental, health, and safety audits, providing a penalty.
- SUMMARY:** This statute amends the Environmental, Health, and Safety Audit Privilege Act, pursuant to an agreement with the Environmental Protection Agency regarding the Texas Environmental Audit program. Specifically, the Act provides that:
1. the privilege against disclosure does not apply to documents if a governmental official charged with enforcement shows a compelling need for the information to protect the health and safety of individuals or the environment;
 2. there will be no immunity for criminal penalties;
 3. if the court finds that a person intentionally or knowingly claimed a privilege for unprotected information, it may impose a maximum fine of \$10,000;
 4. immunity for administrative or civil penalties does not apply if the violation has resulted in a substantial economic benefit for the individual.
- EFFECTIVE:** September 1, 1997.

C. PIPELINES

1. **ACT:** Act of June 20, 1997, 75th Leg., R.S., ch. 1239, 1997 Tex. Sess. Law Serv. 4713 (Vernon).¹⁵¹
- ISSUE:** Disclosure of the location of certain subsurface conditions by a person who is selling unimproved real property to be used for residential purposes.
- SUMMARY:** This law requires a seller of unimproved real property that is to be used for residential purposes to disclose by written notice the location of any subsurface transportation pipeline, injection well, tank, or any facility used or formerly used for the storage or disposal of hazardous waste, natural gas, or petroleum or any other petroleum product.
- EFFECTIVE:** September 1, 1997.
2. **ACT:** Underground Facility Damage Prevention and Safety Act, 75th Leg., R.S., ch. 1407, 1997 Tex. Sess. Law Serv. 5266 (Vernon).¹⁵²
- ISSUE:** Excavation operations that may damage underground facilities.
- SUMMARY:** This so-called "dial before you dig" law requires an excavator to make one telephone call to a statewide

150. To be codified as an amendment to TEX. REV. CIV. STAT. ANN. art. 4447cc.

151. To be codified as an amendment to TEX. PROP. CODE ANN. § 5.010.

152. To be codified at TEX. REV. CIV. STAT. ANN. art. 9033.

toll-free number before beginning excavation. The call will be routed to centers that will inform other underground facility owners of the intentions of the excavator. If one digs before calling, he will pay a fine. If one breaks a pipe, even if he called first, and he does not report having broken the pipe, he will have to pay a fine as well.

EFFECTIVE: September 1, 1997.

3. ACT: Act of June 16, 1997, 75th Leg., R.S., ch. 675, 1997 Tex. Sess. Law Serv. 2288 (Vernon).¹⁵³

ISSUE: The construction and operation of certain sour gas pipeline facilities.

SUMMARY: This law provides that a person may not begin construction of a sour gas pipeline facility before obtaining a Railroad Commission construction permit. A permit applicant must publish notice of the application in a newspaper of general circulation in each county that contains part of the proposed pipeline route. The Commission may issue an order approving the application if it finds that the materials and methods to be used in the construction comply with its rules of safety. Further, the statute defines "sour gas pipeline facility" as a pipeline facility that contains a concentration of 100 parts per million or more of hydrogen sulfide.

EFFECTIVE: June 16, 1997.

D. TAXES

1. ACT: Act of May 23, 1997, 75th Leg., R.S., ch. 208, 1997 Tex. Sess. Law Serv. 1078 (Vernon).¹⁵⁴

ISSUE: Tax exemption for hydrocarbon production from certain inactive oil and gas leases returned to production.

SUMMARY: This Act provides a two-year Inactive Well Incentive by issuing a ten-year severance tax exemption for hydrocarbons produced from a well that has not produced oil or gas for more than one month during the two years preceding the date of application for the exemption. However, previously designated three-year inactive wells are not allowed eligibility as two-year inactive wells. Applications for two-year inactive well certifications are required to be made with the Railroad Commission during the period from September 1, 1997, through August 31, 1999. After February 29, 2000, the Railroad Commission is prevented from issuing such certification.

153. To be codified at TEX. REV. CIV. STAT. ANN. art. 6053-4.

154. To be codified at TEX. TAX CODE ANN. § 202.056(A)(4) and as amendments to §§ 202.056(a)(2), 202.056(b)-(e), 202.056(h), 202.056(i)(2).

- EFFECTIVE: September 1, 1997.
2. ACT: Act of June 20, 1997, 75th Leg., R.S., ch. 1299, 1997 Tex. Sess. Law Serv. 4939 (Vernon).¹⁵⁵
- ISSUE: The joint listing on an ad valorem tax appraisal roll of separate interests in minerals in place.
- SUMMARY: This law resolves questions over the joint listing of separate interests in minerals that are listed on ad valorem tax appraisal roles. A \$500 minimum value for ad valorem taxation on income producing mineral interests was required under prior law. A person with a mineral interest valued at less than \$500 was still taxed if the aggregate value of all separate mineral interests in common property exceeded the \$500 threshold. Now, separate mineral interests which have a taxable value of less than \$500 are exempt from a requirement that separate mineral interests be jointly listed on the ad valorem tax appraisal roles.
- EFFECTIVE: January 1, 1998.
3. ACT: Act of June 18, 1997, 75th Leg., R.S., ch. 931, 1997 Tex. Sess. Law Serv. 2927 (Vernon).¹⁵⁶
- ISSUE: The application of the oil production tax to new or expanded enhanced recovery projects.
- SUMMARY: For oil produced from an enhanced recovery project other than a co-production project, this Act extends the time for applying for the enhanced oil recovery incentive from January 1, 1998, to January 1, 2008.
- EFFECTIVE: May 29, 1997.
4. ACT: Act of June 19, 1997, 75th Leg., R.S., ch. 1040, 1997 Tex. Sess. Law Serv. 3919, 3936 (Vernon).¹⁵⁷
- ISSUE: The administration, collection, and enforcement by the comptroller of various taxes and fees.
- SUMMARY: This section of the Act requires that drilling and completion costs include current and contemporaneous costs associated with the re-completion of high-cost gas wells. The person that is responsible must apply to the Comptroller of Public Accounts for certification for an exemption or reduction. The exemption must be filed with the Comptroller by the later of the 180th day after the first date of production or the 45th day after the date of approval by the Railroad Commission.
- If the application is not filed by the application deadline, the tax exemption or deduction will be reduced by ten percent for the period beginning on the 180th day after the first day of production and ending

155. To be codified as an amendment to TEX. TAX CODE ANN. § 25.12(b).

156. To be codified as an amendment to TEX. TAX CODE ANN. § 202.054(b).

157. To be codified at TEX. TAX CODE ANN. § 201.2037 and as an amendment to § 201.057(f).

on the date on which the application is filed with the comptroller.

Further, neither the Railroad Commission nor the Comptroller may require the disclosure of information relating to receipt reports, delivery points, volumes, rates, or other gas transportation contractual information, unless the disclosure is reasonably necessary for the Comptroller or Railroad Commission to implement or administer chapter 201 or 202 of the Tax Code. This section expires on September 1, 1999.

EFFECTIVE:

September 1, 1997.

5. ACT: Act of June 19, 1997, 75th Leg., R.S., ch. 1060, 1997 Tex. Sess. Law Serv. 4032 (Vernon).¹⁵⁸
- ISSUE: Tax exemptions on oil and gas production.
- SUMMARY: Operators will be entitled to an exemption from the tax imposed by this chapter if they have increased production by marketing gas from an oil well that has been flared for at least twelve months. The Act also provides for a fifty percent oil severance tax exemption for five years for certain incremental production of oil from a lease that averages no more than seven barrels of oil per day. However, if the Comptroller's average price of crude oil reaches \$25 per barrel, in 1997 dollars for three consecutive months, the exemption will be suspended.
- EFFECTIVE: September 1, 1997.

E. GENERAL BUSINESS

1. ACT: Act of June 20, 1997, 75th Leg., R.S., ch. 1432, 1997 Tex. Sess. Law Serv. 5497 (Vernon).¹⁵⁹
- ISSUE: Notice to a payee of a change in the payor of oil and gas proceeds.
- SUMMARY: This Act creates a mechanism to ensure that royalty owners are aware of changes in the payors of their oil and gas proceeds. A new payor must give written notice to each payee for whom the new payor is responsible for distributing the proceeds. The notice must identify the lease or property and give the payor's phone number as well as other items. If the payor fails to notify the payee, the payor is liable for interest at two percent above the amount otherwise prescribed.
- EFFECTIVE: September 1, 1997.
2. ACT: Act of June 20, 1997, 75th Leg., R.S., ch. 1324, 1997 Tex. Sess. Law Serv. 5005 (Vernon).¹⁶⁰

158. To be codified as an amendment to TEX. TAX CODE ANN. § 201.058.

159. To be codified at TEX. NAT. RES. CODE ANN. § 91.407.

160. To be codified as an amendment to TEX. EDUC. CODE ANN. § 66.

- ISSUE: The Board for Lease of University Lands and the leasing, management, and administration of certain public lands, and related fees and penalties.
- SUMMARY: This law rewrites the statute governing oil and gas leases for University Lands. Some of the topics that are discussed are lease maintenance, royalty payments, and audits. This law only applies to future leases.
- EFFECTIVE: January 1, 1998.
3. ACT: Negotiated Rulemaking Act, 75th Leg., R.S., ch. 1315, 1997 Tex. Sess. Law Serv. 4984 (Vernon).¹⁶¹
- ISSUE: Negotiated rule-making by state agencies.
- SUMMARY: This law creates an agency for voluntary negotiated rulemaking of proposed agency rules. Meetings under this Act will be conducted in a manner similar to alternative dispute resolution through mediation between the agency, the public, and the regulated community.
- EFFECTIVE: September 1, 1997.

161. To be codified at TEX. LOC. GOV'T CODE ANN. § 2008.